

Internal Revenue Service

memorandum

CC:TL:N-1361-90

Br2:JMOrenstein

date: DEC - 5 1989

to: Deputy Regional Counsel (TL), [REDACTED] CC: [REDACTED]

from: Assistant Chief Counsel (Tax Litigation) CC:TL

subject: Taxation of Compensation for Lost Fishing Income Due to
the [REDACTED] Oil Spill

By memorandum dated November 15, 1989, you forwarded to this office a copy of a memorandum from [REDACTED] District Counsel to the Associate Chief Counsel (Technical) dated October 27, 1989. In that memorandum, district counsel requested clarification of an opinion regarding whether compensation for lost fishing income due to the [REDACTED] oil spill was subject to self-employment tax. You now request our opinion as to whether the payments made to fishing personnel by the [REDACTED] ([REDACTED]) under the circumstances described below are subject to self-employment tax.

We understand that the district was advising taxpayers that the payments were not subject to self-employment tax. The [REDACTED] district, on the other hand, has been advising taxpayers that the payments are subject to self-employment tax.

ISSUE

Whether payments from [REDACTED] to compensate the fishermen for their lost profits as a result of the [REDACTED] oil spill are includible in computing net earnings from self-employment pursuant to I.R.C. § 1402(a).

CONCLUSION

Although we share your concerns, we believe that an objective legal analysis leads to a conclusion that the instant payments are subject to self-employment tax. We find significant points of distinction between the factual scenarios discussed herein and that discussed in Newberry v. Commissioner, 76 T.C. 441 (1981), such that Newberry, while a looming hazard, is not a bar to successful litigation of this issue.

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FACTS

The payments in question were made by [REDACTED] to compensate individuals who have been self-employed fishing personnel in prior years. As a result of the [REDACTED] oil spill from the [REDACTED], these individuals suffered losses in fishing income for [REDACTED]. There are two types of claimants: (1) the boat owners who own limited entry permits to fish (permits that allow the holder to fish for a specific kind of fish using a particular method for a designated geographic area and period of time), and (2) crewmen who work for shares of the catch. In order to prevent thousands of individual suits, [REDACTED] has set up a claims office and instituted a simplified claims procedure to settle the claims of [REDACTED] who suffered losses because of the spill. [REDACTED] currently is making interim or final settlement payments on claims for fishing income lost by captains and crewmen who were prevented from fishing in [REDACTED]. It is [REDACTED] District Counsel's understanding that, before any settlement payment is made, [REDACTED]'s claims adjusters require proof that the claimant had earned a certain level of income from fishing in prior years and that he or she was ready, willing, and able to fish in the current year.

According to district counsel, most of the crewmen claimants did not fish in [REDACTED] because of the oil spill, although some may have participated in some unaffected fishery during the year. Most of the boat owners that were prevented from fishing have reportedly hired themselves and their boats to [REDACTED] for the cleanup of the spill. Thus, these boat owners will apparently report their income and expenses from the charter activity on Schedule C, Profit or Loss from Business. The payments from [REDACTED] for services performed by crewmen and owners in the cleanup are not at issue in this memorandum.

[REDACTED] District Counsel's position is that, because the payments from [REDACTED] are payable expressly on the condition of and only to the extent that the claimant's normal trade or business (fishing) was not carried on, Newberry requires a determination that the payments are not subject to self-employment tax. They have requested that we concentrate our analysis on the "typical" situation, where a taxpayer who has historically earned a major portion of his or her income from fishing, "was unable to fish at all in [REDACTED]." For purposes of our analysis, we are also assuming that the taxpayer has been self-employed in the performance of the fishing services in the prior year.

You are concerned that the situation described above will not provide a "clean" litigating vehicle because thousands of taxpayers in varying factual circumstances are receiving the

subject payments. You are also concerned that the reputation of the [REDACTED] district may be damaged if their published position is now reversed.

DISCUSSION

After a careful analysis, we have concluded that the payments from [REDACTED] to compensate fishermen for lost profits as a result of the [REDACTED] oil spill are includible in computing net earnings from self-employment pursuant to section 1402(a). The legal basis for our conclusion may be found in the attached memorandum to the Acting Assistant Chief Counsel (Employee Benefits and Exempt Organizations).

We agree with your concern that our conclusion may embarrass the [REDACTED] district. However, a contrary conclusion would no doubt embarrass the [REDACTED] district. In any event, an objective legal analysis must dictate our response.

We also appreciate your concern that there will be varying factual circumstances such that it will be difficult to find a "clean" litigating vehicle that will decide the issue with respect to all recipients of the subject payments. However, if the government can prevail in a case involving a fisherman who received payments and did no fishing at all during [REDACTED], then we believe the hazard embodied in Newberry will have been overcome and the government will have a substantial chance of prevailing in all of the other cases despite varying factual scenarios.


Finally, we note your concern that our conclusion may appear to recant our eight year implied "acquiescence by silence" in Newberry. We believe there are significant points of distinction between Newberry and the factual scenarios discussed herein so that this concern may be allayed. However, we do indeed contend that Newberry was incorrectly decided. This contention is consistent with Respondent's Motion for Reconsideration and Revision of Opinion and supporting memorandum with respect to Newberry filed with the Tax Court on April 9, 1981. The motion was, of course, denied by Order dated May 4, 1981.

Perhaps the decision should have been appealed in 1981 or, at least, an Action on Decision drafted to reflect nonacquiescence.¹ However, failure to act at the time Newberry was decided should not necessarily be taken to mean that the Service is forever barred from revisiting the issue. Consequently, litigation of a case arising in one of the instant scenarios may provide an opportunity to erode Newberry and address the issue anew.

If you have any question please contact Jeffrey Orenstein at FTS 566-3289.

MARLENE GROSS

By:


DANIEL J. WILES
Acting Deputy Assistant Chief
Counsel (Tax Litigation)

Attachment:

Memorandum to Acting Assistant Chief Counsel (Employee Benefits and Exempt Organizations)

cc: [REDACTED] District Counsel

¹ Interestingly, the records of the Appellate Section of the Tax Division, Department of Justice, indicate that Newberry was referred for appeal consideration. However, no memorandum for the Solicitor General was prepared and, obviously, no appeal was taken. We are not able to ascertain why no appeal was ever taken.